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The Angel Investor Market In 2005, Q1 And Q2: The Angel Market Sustains Investment Levels

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THE ANGEL INVESTOR MARKET IN 2005, Q1 and Q2: THE ANGEL MARKET SUSTAINS INVESTMENT LEVELS

Market Size

The angel investor market has shown signs of maintaining investment levels in the first half of 2005, with total investments of \$11.0 billion, according to the **Center for Venture Research** at the University of New Hampshire. These investments are slightly less than the first half of 2004 (\$12.4 billion) but on track to match 2004 investments of \$22.5 billion. A total of 26,000 entrepreneurial ventures received angel funding in the first half of 2005, a level comparable to the first half of 2004. The number of active investors in Q1-2, 2005 was 126,000 individuals, a slight decline from Q1-2, 2004. An average of 4-5 investors joined forces to fund these entrepreneurial ventures.

Stage

Angels continue to be the largest source of seed and start-up capital, with 48% of the first half of 2005 angel investments in the seed and start-up stage. While this preference for seed and start-up investing is the largest stage for angel deals, this also represents an 11% decline in this stage from Q1-2, 2004. While angels are not abandoning seed and start-up investing, it appears that market conditions, and the preferences of large formal groups of angels, are resulting in angels engaging in more later stage and follow-on funding for their investments. New, first sequence, investments represent 69% of Q1-2, 2005 angel activity. This shift in investment strategies toward post seed investments reduces the proportional amount of seed and start-up capital. This restructuring of the angel market has in turn resulted in fewer dollars available for seed investments, thus exacerbating the capital gap for seed and start-up capital in the US.

Yield Rates

The yield (acceptance) rate is defined as the percentage of investment opportunities that are brought to the attention of investors that result in an investment. The peak yield rate of 23.3% occurred during the height of the investment bubble in 2000. Since that peak the yield rate has stabilized at around 10%. In 2004, yields increased to 18.5% from the previous year's yield rate of 10.3%. In the first half of 2005 yield rates continued this upward trend and rose to 21.8%. A continued departure in yield rates from the historical average could be troubling if this rise can be attributed to an influx of inexperienced angels.

Sector Analysis

The life sciences commanded the greatest attention, with 20% of total angel investments in Q1-2, 2005 in healthcare services/medical devices and equipment, followed by biotechnology, with a 17.5% share of angel investments. Close behind were software investments (17%) and IT services (13%). The remaining investments were approximately equally weighted across high tech sectors, with each having between 3% and 6% of the total deals. This market level sector diversification indicates a robust investment pattern and provides a foundation for reasonable growth in the market. Since the angel market is essentially the spawning grounds for the next wave of high growth investments, this sector diversification provides an indication of investment opportunities that will be available for later stage institutional investors.

Sector	Health	Biotech	Software	IT Services	Hardware	Semiconductors /Networks	Fin Services
Deals	20%	17.5%	17%	13%	6%	5%	4%

Market Participation

If the angel market is to achieve sustainable growth there needs to be a reasonable augmentation in active investors, and thus, level of participation is an important consideration. While the number of individuals that are members of organized angel groups are increasing, there is a larger percentage of latent angels (individuals who have the necessary net worth, but have not made an investment). In Q1-2 2005, 66% of the membership in angel groups were latent angels (as compared to 56% in 2004 and 48% latent investors in 2003). This increase in latent investors over time indicates that while many high net worth individuals may be attracted to the early stage equity market, they have not converted this interest into direct participation. This lack of active involvement may be the result of the current trend to rush to form angel groups, rather than meeting the more basic systemic need for educational programs and research to move the latent angel to the active investor.

The **Center for Venture Research (CVR)** has been conducting research on the angel market since 1980. The CVR's mission is to provide an understanding of the angel market and the critical role of angels in the early stage equity financing of high growth entrepreneurial ventures. Through the tenet of academic research in an applied area of study, the CVR is dedicated to providing reliable and timely information on the angel market to entrepreneurs, private investors and public policymakers.

The Center for Venture Research also provides consulting services to angels, angel groups and state and foreign governments. For more information visit www.unh.edu/cvr or contact the CVR at 603-862-3341.